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BY THE SENATE.

FEBRUARY 25, 1870.

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By order,

AUGUSTUS GASSAWAY,
Secretary.

REPLY

OF THE

Attorney General of Maryland,

TO THE

ORDER OF THE SENATE.

Upon the Subject of the Payment of \$58,000.

BY THE

CHESAPEAKE & OHIO CANAL CO.

TO THE

Commonwealth of Virginia.

ANNAPOLIS.

WILLIAM THOMPSON & B., STATE PRINTER.

1870.

STATE OF MARYLAND,

ATTORNEY GENERAL'S OFFICE,

Baltimore, March 5, 1870.

To the Honorable,

The Senate of Maryland:

GENTLEMEN:—I have the honor to acknowledge the receipt of a copy of your order of yesterday, "that the Attorney General of Maryland be requested and directed to investigate the circumstances under which the sum of \$58,000, or more, was recently paid by the Chesapeake and Ohio Canal Company, to the State of Virginia, and give his opinion, in writing, as to whether the said payment was or not an illegal misapplication of the funds of the said Company, and a violation of the rights of this State as mortgagee of the revenues of said Company, and report to the Senate at an early day."

In reply, I most respectfully submit, that at this late period of the session, it would be impracticable to commence such investigation in the hope of reporting the result at an early day. I can, therefore, give to the Senate only such information concerning "the circumstances under which" the payment was made, as I possess. This I proceed to do in the following statement:

In December, 1867, "the Commonwealth of Virginia," by her Attorneys, filed a bill in the Circuit Court of Baltimore city, against the Chesapeake and Ohio Canal Company and certain trustees and bondholders, the chief object of which, (as stated in the brief of its counsel, at the argument on the 22nd of June, 1868,) was to obtain a decree of a Court of competent jurisdiction, with all the necessary and proper parties before it, determining the legal priorities of the various creditors of the Chesapeake and Ohio Canal Company, so that it may, with safety, pay its surplus tolls and revenues to the persons legally entitled to receive them.

The claim set up by Virginia in the bill was, that as guarantor of \$300,000 of "the preferred bonds," of \$200,000 of the repair bonds, issued by the Company, as it was alleged, in virtue of the Maryland Act of 1844, chapter 281, (whereby it was charged that Maryland waived her priority as mortgagee under previous mortgages of the tolls and revenues of said Company, in favor of the said bonded debt and interest,) Virginia had paid and taken up certain coupons of interest on the repair bonds, in default of the Company's being able to pay the same. That the Company being also unable to pay the interest on the preferred bonds, made an arrangement with Seldon, Withers & Co., bankers, under which they took up certain coupons of interest to the amount of \$143,000, for \$140,000, of which, the Company afterward issued to them *certificates of debt bearing interest payable semi-annually*, whereby they claimed to be subrogated to the rights of the original owners of the coupons. That Virginia, as assignee, for value, holds the said certificates, which she claimed to be a lien upon the tolls and revenues of the Company by virtue of the Maryland Act of 1844, chapter 281, and the Company's mortgage to certain trustees. That Virginia had also paid interest coupons on preferred bonds as guarantor, which it had surrendered and for which it received a certificate of indebtedness of the Company for \$35,000, bearing interest from 1st October 1852, payable half-yearly. That in addition, Virginia, as such guarantor, had paid other coupons of interest to the amount of \$269,625. Upon all these claims, the bill averred that Virginia was entitled to interest from the time of the said several payments, to the payment of which, the net tolls and revenues of the Company should be applied: charging that the Company had misapplied its funds, but had then on hand \$100,000, of net revenue, which ought to be applied to said claims.

The said "Trustee," and certain holders of repair and preferred bonds, were also made defendants.

The Canal Company, by its counsel, (of whom I was one,) filed its answer, which, in substance, admitted the legislation of Virginia and Maryland, and the issue of the preferred and repair bonds, and the guarantee by Virginia, as alleged.

It admitted that, as guarantor, Virginia had paid interest, but that the Company being ignorant of the amount, prayed "that the complainant may be required to furnish proof thereof;" it admitted its inability to pay the interest coupons as they fell due, but insisted that its inability was without the fault of the respondent; it admitted that it "borrowed money of Selden, Withers & Co.," to pay interest on said bonds, "pledging the future revenues of the Company, *subject to existing priorities, for the repayment of said money*;" but "refers to said agreement between it and said firm, when produced, for the terms thereof;" admitted the issue of certificates of indebtedness to Selden, Withers & Co., but did not "admit that they have become the property of the complainant, but insisted on proof thereof;" and submitted "the legal rights of the complainants as holder, when that fact shall be proved" to the Court; admitted its failure to pay interest coupons, and called for proof of sums paid by complainant as guarantor; admitted the issue of certificate for \$35,000, but left complainant to prove present ownership. The answer submitted to the decision of the Court, the claim for interest upon the said certificates, and upon amounts paid by complainant for redemption of interest coupons, "upon proof of such payments, and upon the proper construction of the contracts and obligations, under which said payments were made, and upon the true construction of the powers and obligations of this respondent in the premises." It further submitted, that in order that it may be fully protected in any decree that may be passed, and that the rights of all parties may be duly regarded, whether or not, the creditors of the Potomac Company, and the State of Maryland should be parties to this suit," and asserted its willingness and readiness to apply its surplus revenues, "in such manner as may be deemed lawful and right, in view of its powers, duties and obligations, and in view of the rights, powers and obligations of all persons concerned."

The other defendants having answered, the case was argued in June 1868, and subsequently, upon the Court's decision that the State of Maryland was a necessary and proper party, the complainant obtained an order to serve a copy of the bill upon the Governor, the Board of Public Works, and

the Attorney General, requiring that the State should become a defendant in the suit.

Each of those agents of the State separately answered that the State had conferred upon them no such authority, and that the General Assembly only could authorize the appearance of the State, as a defendant, in its own Courts: that it was manifest upon the face of the bill, that the State of Maryland was an indispensable party to the adjustment of priorities in the payment of the surplus tolls; that the complainant was bound to know the law of the forum to which it appealed; that a session of the Legislature had been held and adjourned without any notice or application to the State to become a party, and that the complainant must submit to the consequences of delaying the proceeding until another session of the Legislature should be held.

Upon these answers the cause was again heard in March, 1869, and on April 10, '69, the Court filed its opinion sustaining the ground taken in the answers, and passed an order to stay the proceedings accordingly.

This was the state of the case when in December last it was stated in the public press that the Company had paid to the State of Virginia \$58,000.

Having been informed, a few days after, that I would probably be called on for an official opinion upon the subject, I requested the Comptroller to obtain for me a copy of the proceedings of the Company, in order that I might know on what account the payment was made. In accordance with this request, the Clerk of the Company furnished me with the copy of the proceedings, which I beg to submit herewith to the Senate, as containing all the information I have upon the subject. No request for any opinion was made of me until that contained in the order of the Senate, except some inquiries of the present Comptroller as to the power of the Canal Company to fund the unpaid interest coupons, so as to make them to bear interest, and give such funded debt priority over the debt due by the Company to the State, &c., to which I replied on the 23d ult.

In reply to the request for my opinion upon the legality of the payment out of the net revenues of the Company, I have to state that I am not informed of the particular claims to which the payment was applied, so as to form an opinion upon them

all. I have addressed a note to the President of the Company, requesting a statement, and when I shall have received it, I may be able to answer more fully. But I infer from "the agreement" in the proceedings herewith sent, that a part of the sum so paid was applied to pay interest on the bonds for \$140,000, to Selden, Withers & Co., and part to pay interest to 1st October, 1869, upon the certificates for coupons funded in 1853. I have heretofore considered the question as to the character of such bonds and certificates in connection with the Act of 1844, chapter 281. The Court of Appeals in *Brady vs. The State*, 26, Md. Reps. 308, construing the Act of 1844, ch. 281, said "The State waived its priority only in favor of the liens created and authorized by that Act." The net tolls were relied on to pay the interest coupons, and the principal of the bonds so authorized.

The State stipulated that "in no case should it be bound or held responsible for the payment of the bonds or interest thereon," issued under the Act. Those who took the bonds relied upon the accruing net tolls to pay the semi-annual interest. If no net tolls are in hand to meet the coupons when due, the holders are entitled to be paid whenever afterwards net tolls shall be in hand. But if, instead of retaining the original security, with its specific lien issued under 1844, chapter 281, they give up the coupons to the Company and accept in lieu thereof new bonds, bearing semi-annual interest, I am of opinion that such bonds are not within the waiver of the State of Maryland; that they create but a general indebtedness, and are postponed to the holders of the original bonds and interest coupons; and also to the debt due to the State on its mortgages. The Company was incompetent, without the assent of the original lien bondholders, and of the State, to enter into the new contract and give it priority over such original bondholders, and over the debt due to the State of Maryland. The effects of allowing these new bonds for interest, bearing interest payable semi-annually, to retain the lien of the surrendered coupons, is to give compound interest to the holders, to the prejudice, immediately, of the holders of the original bonds, and remotely, to the rights of the State as mortgagee.

I am, therefore, of opinion, that to the extent of any pay-

ment to Virginia of interest upon these new bonds, the Company misapplied its net revenues. I have been informed, however, by one of the present counsel of the Company, that an agreement has been entered into with the Virginia authorities, whereby the money received shall be applied according to the ultimate decision of the Courts in the pending case.

From the foregoing, the Senate will perceive the reason of the Court's decision, that the State of Maryland has such an interest in the subject matter of the pending suit, that it was indispensable to justice that it should have the opportunity of becoming a defendant therein, and that this could be done only by an Act of the General Assembly authorizing it.

Accordingly, on the 3rd instant, I received a copy of the Act recently passed, directing the Attorney General to cause the State to be made a defendant in the said suit, and in any other suit now pending, or hereafter to be instituted, the object of which shall be to determine the proper application of the net revenues of the Company. Provision is therein also made for a speedy hearing of the case in the Court of Appeals. And the 3rd section enacts, "that in no event shall the State of Maryland be held liable for any costs that may accrue in this case, or in any case that may arise under the provisions of this Act. The State of Maryland has invested in the Canal Company a sum, principal and interest, of about twenty millions of dollars. Every citizen, and especially every tax-payer, is interested in its being made productive as soon as possible. It has an interest involved in the decision of this question of compound interest, of perhaps a half million of dollars. It has mortgages upon the entire work, property and revenues of the Company, waived only to the extent of the Act of 1844, chapter 281. It asks to be made a defendant to defend its rights involved in that waiver. It comes not as a sovereign State, but as a creditor, seeking with other creditors, a decision of its own Courts upon its rights under laws and contracts, but declines to be liable, as other creditors and parties to the same suit are, for the usual costs incident to its defence, such as copies of its mortgages and other documents necessary to be exhibited with its answer, Clerks' fees, printing of briefs, &c. I feel sure the pro-

vision originated in a misconception of the purposes of the suit, and of the interest of the State as creditor involved in it, and not with a purpose or expectation of embarrassment to the Court or to its officer in the discharge of the duty required of him. I was upon the point of addressing a note to a member of the General Assembly upon this subject, when I received the order of the Senate, to which I have been compelled to make a more hurried reply than I desired, and in doing so, beg most respectfully to invite their attention to the provision of the Act, to which, with reluctance and regret, I have deemed it my duty to advert. It is most respectfully submitted, that if the interest of the State in the controversy be deemed of sufficient importance to be defended, it is due to the Court and to the dignity of the State, that its request to be admitted as a defendant, shall not be coupled with a condition of special exemption from the incidents which belong equally to all parties to suits, and for which provision is made in all other cases in which the State is a party.

Very respectfully,

Your obedient servant,

ISAAC D. JONES,

Attorney General.

LETTER TO THE COMPTROLLER.

STATE OF MARYLAND,
ATTORNEY GENERAL'S OFFICE,
Baltimore, 23d Feb., 1870.

Hon. L. Woolford, Comptroller:

DEAR SIR:—In reply to the inquiries in your letter of 19th inst., I have the honor to state, first, as to the power of the Chesapeake and Ohio Canal Company to fund the unpaid coupons of the preferred and repair bonds so as to make them bear interest, and give such funded debt priority over the debt due by the Company to the State of Maryland, I am clearly of opinion that the Company has no such power. Admitting for the sake of the argument, that the repair bonds as well as the preferred bonds, were authorized by the Act of 1844, to take priority of the State's debt, the extent of the State's waiver was to the *net revenue and tolls* to pay the interest and provide a fund to redeem the principal, with an express proviso that the "State shall, *in no case*, be bound or held responsible for the payment of the said bonds or of the interest thereon." Those who took the bonds knew well that until there accrued net revenues and tolls they could get nothing. When such tolls are in hand they are applicable to pay the interest in arrear. But there is no authority to compound the interest to the prejudice of the State. The bondholders got passed chapter 359, of 1867, which required the Company to issue certificates for such funded debt, bearing interest. But the Board of Public Works refused to execute it, and on appeal to the Constitutional Convention, after full debate upon this very point, the Convention declared the Act to be *null and void*. So unanimous was the vote that not even a division was called for. See memorials of bondholders, proceedings of Convention, 1867, page 317 to 324. Report of Com. on Public Works, page 391, &c., &c., votes &c., thereon, page 688 to 703. In the case of

Brady *vs.* The State, 26 Md. Reps., 300, will be found an exposition of the Act of 1844, chapter 281, by the Court of Appeals. It will be seen, page 300, that at the instance of the Board of Public Works, the State got an injunction *vs.* Brady, an attaching creditor, and the Company, restraining the Company from paying any debts from net revenues to any creditors not entitled to claim payment in priority of the State. And on page 308, the Court say: "The State waived its priority only in favor of the liens created and authorized by that Act," viz.: 1844.

2d. As to the case now pending in this city, State of Virginia *vs.* The Canal Company and others, if prosecuted to final hearing, after the State shall become a defendant, the extent of the State's waiver and of the rights of all classes of bondholders, may be adjudicated. The Company, in its answer to the bill of Virginia, submitted all the questions arising out of Virginia's claims, including that of interest on certificates for interest and coupons, to the decision of the Court. But the agreement of certain bondholders, which the Company adopted, last December, as the basis for the appropriation of \$160,000, as I recollect it, yielded every claim of Virginia so fully, that a part of the arrangement was that Virginia should dismiss the pending bill. I have been since informed by Col. Marshall, one of the counsel of the Canal Company, that another agreement has been entered into whereby the case is to be prosecuted to final decree.

3d. "Can the holders of the said bonds recover interest against the Canal Company on the over-due coupons from the date of their falling due?" As I have already stated, I think they cannot, as a debt entitled to priority over the State of Maryland.

4th. "What legislation is necessary to protect the State's interest against the attempt which may be made to fund the said interest to the prejudice of the State?" It does not occur to me that any additional legislation is required. The Constitution has entrusted the State's interest in the public works to the Board of Public Works. That Board has the power in stockholders meeting to appoint the President and Directors of the Company, and afterwards to supervise their proceedings. The Board has the right to be informed before

any action is taken which affects the interest of the State as creditor or stockholder of the Company. And if it has good reason to apprehend that acts are about to be done prejudicial to the State's interest, it can cause proceedings to be instituted in the name of the State to protect such interest, as was done in the case of Brady in 26 Md. before referred to. The Convention of 1867, after full consideration, determined that the State's interest in these works could nowhere be so safely entrusted as in the Board of Public Works, and refused by repeated votes and by large majorities, to subject it to legislative control. It is true, that to make the State a defendant in her own Courts, requires express authority of law. I understand an Act has been passed at the present session, authorizing the Attorney General to appear for the State in pending cases against the Canal Company. I am not informed, however, of the exact terms of the Act.

Very respectfully and truly,

ISAAC D. JONES,

Attorney General of Maryland.

